

OCT - 2 1991

Maggie Bezerra
Tax Haven Group

Special Counsel (International) CC:INTL

[REDACTED]
[REDACTED] Last month we discussed your proposed write up concerning [REDACTED], an 1120 company.

[REDACTED] paid organization expenses, start up cost and related travel expenses to form offshore trusts and alleged insurance companies in Barbados and the Cayman Islands. Additional funds were paid for insurance licenses.

Purported insurance premiums went from [REDACTED] or from individual [REDACTED] through a Laguna Niguel consulting company to the offshore insurance companies. A portion of the insurance premium was used to fund reinsurance with an unknown offshore entity. The residual (total insurance premium minus reinsurance portion) was sent to an offshore trust. The beneficiary of the trust is usually the oldest living relative of the [REDACTED]-settlor.

I agree with the approach you are taking, denying deductions under I.R.C. § 162 for the organizational costs, and treating them as either contributions to capital or expenditures that must be amortized.

With respect to the insurance premium, you have asserted that the taxpayer has failed to establish that the Barbados company is an insurance company, and consequently have disallowed the deduction.

I suggest you conduct further interviews with the [REDACTED] purportedly covered under the insurance policies, in order to establish whether or not any claims have been paid. If claims have been paid your disallowance of the deduction for the payment of the insurance premium could fail.

You may want to consider whether in substance, the insurance company is a captive, i.e., that it is really a self insurance scheme. It may be that Barbados company has a separate accounting scheme in which [REDACTED] separate accounts are kept, one for each [REDACTED]. If for example, a claim were paid by the insurance company of \$50,000, the capital account of

008133

the [REDACTED] for whom the claim was paid might be negative requiring a \$50,000 contribution to replenish it. This would be indicative of self insurance and the principles of Rev. Rul. 77-316 could apply.

Finally, through the rebate of premiums through the respective [REDACTED] trusts, it seems you have, at a minimum, established that the premiums paid were greatly inflated. To the extent the premiums paid by the [REDACTED] or their professional service corporations exceed arm's length amounts, a denial of the excess amount is a viable fallback position to a total denial of the premiums under either of the first two alternatives.

Regarding the treatment of the premium payments by the professional corporations as constructive dividends to the dentist, you should exercise caution. If the [REDACTED](s) is (are) employees of the corporation, it would seem the corporation has an insurable interest and may have a valid defense that the payment was to protect the corporation from tort or malpractice liability.

Regarding amounts received by the respective [REDACTED] trusts (rebates from the Barbados insurance company) these are properly includable in the respective incomes of the [REDACTED] if you are able to establish the trusts are grantor trusts. At this point you have circumstantial evidence that this is the case. You may want to obtain the advice of District Counsel on this point.

Since our ongoing discussions began about a year ago, District Counsel Los Angeles has appointed Joyce Sugawara who I understand is reviewing your case. I shall forward a copy of this memo to her. You should understand that Joyce has final say on all matters involving Counsel's advice to you.

If I can be of any further assistance, please don't hesitate to call me at (202) 377-9493.



KIM A. PALMERINO

cc: Joyce Sugawara
Bill Bonano